Fed Board

Christopher Waller, Q&A Segment

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Zoom Transcript (Christopher Waller Answers Only)

Question
So you see the balance sheet going forward with both short and long term treasuries in it or do you think that it will be liquid enough or you can have to do it just with the short term.

Christopher Waller
Yeah, so one of the things we used to have a very short dated, balance sheet. We typically buy very short term stuff that would run off quickly. We could buy it, let it run off whether by runoff.

During the last decade when we were trying to get the economy recovering after the great financial system, we started moving into longer data maturities to try to put downward pressure on longer-term interest rates.

That spills into mortgages, all sorts of things. From with long duration assets, their long duration, once they're on your balance sheet, you've got it for a long time. So we did that, but you know, over time we're gonna try to bring that maturity structure back down. And then the agency back MBS that we have on our balance sheet. I'm not a fan of this.

I've made this is nothing new. People have heard me talk about this before. I don't like that we are buying these things. They have very long dated. You think about a mortgage back security with a 30 year Mortgage is underneath it.

You're gonna own that thing for a long time or rolls off your balance sheet. So I don't really like that we have that asset. It's a little too much concern for me, but. Hopefully we at some point can kind of run those off and Never get into the business of buying, mortgage back securities again.

Question
It's inverted. It's inverted. As Peter said, when you look back over the last. 40, 50 every time the yield curve is inverted within 6 to 12 months. There's a recession.

Christopher Waller
So markets are very keen on looking at the yield curve inversion. So I try to make the case that they're good in versions and they're bad in versions. And we haven't seen a good one for a long time and maybe that's what we're looking at.

So the idea is this. When there's yield curve inversion. Long term rates are below current short rates. That's what Peter showed you in the graph. Now standard kind of model in economics would say the long rate is the average of all the future short rates. So if the long rate is below the current short rate, it's because the markets believe interest rates are gonna come down in the future.

There's 2 reasons those interest rates could come down. One is real returns are bad. Growth is bad. The economy is bad. And the Fed cuts interest rates. That's kind of what's been in the past. And that under that story is inflation is fairly constant. Because interest rate compensates you for a real return and expected inflation.

And if expected inflation is at or near our 2% target for 40 years. The only time you see the inversion, it's got to be the real part is looking bad. Growth is looking bad. The economy is looking bad. What's the situation we're in today? We've got very high inflation. We haven't seen that since the late seventies, early eighties. But everybody thinks what's gonna happen to inflation. It's gonna come down. So if you think inflation is gonna come down, interest rates will come back down with it.

That's a good inversion. So that's what I'm thinking right now is what you're seeing in the inversion is not so much fears about bad economic outcomes in the future, but beliefs and trust that we're going to bring inflation back down and rates will be lower in the future once we do that.

Question
Regarding Inflation

Christopher Waller
I'm on my job trying to get inflation down. You may, some people may not like how interest rates other people's may like them. There suddenly depositors in the US are suddenly saying for the first time in a decade, hey, I can actually earn some money on my savings account. So, you know, that's the main focus I have in my job is to get inflation back down to 2%. Inflation is a tax on people as Peter was talking about. And the higher that inflation rate is, the higher that taxes on your normal income and your nominal well. So. The job is to get it down, keep it stable to the point where you don't even think about it anymore.